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No. 573

In the Supreme Court of the United States

OCTOBER TERM, 1931

NORTH AMERICAN OIL CONSOLIDATED, A CORPORATION, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT

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In the Supreme Court of the United States

OCTOBER TERM, 1931

No. 575

NORTH AMERICAN OIL CONSOLIDATED, A CORPORATION, petitioner

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH DISTRICT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 130–145) is reported in 12 B. T. A. 68. The amended opinion of the Circuit Court of Appeals (R. 194–203) is reported in 50 F. (2d) 752.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 15, 1931. (R. 193–194.) Petition for rehearing was filed July 15, 1931, and was

denied September 14, 1931. (R. 194.) Petition for a writ of certiorari was filed December 14, 1931, and granted January 25, 1932. (R. 205.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

STATUTES AND REGULATIONS INVOLVED

The applicable statutes and regulations are set forth in Appendix A, *infra*, pp. 35–40.

QUESTIONS PRESENTED

1. Whether a receiver directed by court order to take charge of a part of the property of the petitioner corporation and impound the receipts arising from oil wells on such property pending the settlement of litigation between the petitioner and the United States was required by Section 13 (c) of the Revenue Act of 1916 to file an income-tax return in respect of such income impounded in 1916.

2. If the receiver was not required to report such income, whether it was taxable to the petitioner for 1916 when the income was impounded, for 1917 when it was released to the petitioner and the receiver discharged, or for 1922 when the litigation was terminated.

STATEMENT

The petitioner is a California corporation. During all of the years involved it was engaged in the production of oil and derived income from many

parcels of land. (R. 92–111.) On July 15, 1913, the petitioner acquired Section 2, Township 32, Range 23 East, M. D. B. & M., Kern County, California. (R. 116.) Legal title to the land in question was in the United States and it was included within the area described in the presidential withdrawal order of September 27, 1909. Prior to November 30, 1915, the United States instituted suit in the United States District Court for the Southern District of California to oust petitioner from possession of this property and on February 3, 1916, the court entered an order appointing a receiver to operate or supervise the operation of the oil wells on this property and to receive the income arising therefrom. (R. 116–120; *United States* v. *North American Oil Consolidated*, 242 Fed. 723.)

On June 5, 1917, the order appointing the receiver was vacated by final decree of the District Court (R. 120) and the bill was dismissed (242 Fed. 723). The Government appealed and the Circuit Court of Appeals affirmed the decree of the lower court (264 Fed. 336). The case was brought to this Court where the appeal was dismissed under a stipulation of counsel (258 U. S. 633). See mandate of March 21, 1922. (R. 120–122.) On April 12, 1922, a patent to Section 2 was issued by the United States to certain applicants who had agreed to convey to the petitioner.

During the period February 2, 1916, to December 31, 1916, the receiver collected and impounded net

income from the oil wells on the property amounting to $171,979.22. (R. 123, 164.) Petitioner occupied the land and operated the wells under authority of the receiver. The receipts were entered on the books of the petitioner as its income, were not reported as income in its original return for 1916, but were so reported in an amended return filed in 1918. (R. 122.) These receipts were actually turned over to the petitioner in June, 1917, at the time of the District Court's decree. (R. 123.)

Upon auditing the petitioner's income and profits tax returns for 1917, the Commissioner determined a deficiency of $109,239.61, the deficiency being based on other items. (R. 20–30.) The petitioner appealed to the Board of Tax Appeals. In an amended answer to the amended petition filed January 29, 1927, the Commissioner prayed that the deficiency be increased to include the tax on the impounded income paid over by the receiver in that year. (R. 45–48.) In this answer it was stated that the amount of the impounded income was $253,150.96 instead of $171,979.22, but this latter figure was given in the stipulation filed with the Board. (R. 164.)[1]

The Board of Tax Appeals held that the sum in question was not taxable to the petitioner in 1917

[1] The difference between the two sums apparently represents the income received by the receiver after December 31, 1916.

In the memorandum for the respondent in response to the petition for certiorari, page [illegible] it was erroneously stated that the Commissioner prayed for an increase in the deficiency to $253,150.96. The amount should be $128,619.36. (R. 150.)

but was taxable to the receiver in 1916 irrespective of whether the petitioner was on the accrual basis or on the cash receipts and disbursements basis, and found a deficiency of only $35,806.30. (R. 145–146.)

Upon appeal to the Circuit Court of Appeals for the Ninth Circuit that court reversed the decision of the Board, holding that the receiver, as a receiver of only a part of the property of the petitioner, was not required to file a return in its behalf for 1916, and that the income was taxable to the petitioner for 1917 rather than for 1916 or 1922. (R. 194–203.)

SUMMARY OF ARGUMENT

1. The receiver was in charge of only part of the property of the corporation during 1916.

The language employed in Section 13 (c) of the Revenue Act of 1916, *infra*, indicates that it is only receivers in charge of all of the property or business of a corporation who are required to file returns of income, and the regulations have so construed that provision and similar provisions of later acts. This settled administrative construction of similar statutory provisions is entitled to great weight, particularly in view of the reenactment by Congress of such provisions.

The administrative construction is reasonable. There is no provision for consolidation of return of the receiver of a part of a corporation's property or business and the return of the corporation itself.

2. The Board held it to be immaterial whether the taxpayer filed its returns on the cash basis as the receiver was taxable on the impounded income. The Circuit Court of Appeals reversed the Board holding that the income was taxable to the corporation for 1917 irrespective of the basis on which it filed its returns.

The Board should have made a finding to the effect that the taxpayer filed its returns on the cash receipts and disbursements basis since the returns so indicated (R. 169, 178), the petitioner introduced no evidence to the contrary and the only thing in the record to the contrary was an inconclusive statement in the deficiency letter. (R. 23–24.) Even if the burden of proof as to this issue was upon the Commissioner due to the fact that the question of the taxability of the impounded income was first raised in a claim for increased deficiency asserted before the hearing in accordance with Section 274 (e) of the Revenue Act of 1926, the Commissioner sustained the burden of proving that they were made on the cash basis. If, therefore, the decision in this case turns upon this issue, the respondent should prevail.

Under either system of accounting the income was taxable for 1917.

(a) The cash receipts and disbursements method of accounting requires that a taxpayer report income actually received in cash or its equivalent. In the instant case the income was actually received

during 1917 when the receiver was discharged and the impounded receipts released.

While the oil was produced in 1916, there was at that time no receipt by the petitioner of the proceeds of the sales, and no knowledge on its part as to whether the receipts would be paid to the Government or to it. Nor was there any constructive receipt of the income in 1916. There is nothing in that theory which requires a taxpayer to report income which it may never receive. Nor is the case taken outside the rule that a taxpayer on the cash basis must report income for the year in which it was actually received by the fact that the Government was claiming the receipts in 1917 and continued to claim them until the litigation was finally settled in 1922. Such a theory would be contrary to the principle that the income tax is imposed for a yearly period. Where a taxpayer on the cash basis receives income under a claim of right without restriction as to his disposition of it he is required to report the amount even though claims against the income are being asserted and he may ultimately have to pay an equivalent amount to another. The situation of this taxpayer in 1917 is the antithesis of the situation presented in *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359, where the Court held that a taxpayer should report damages as income when he actually receives them.

(b) The accrual of income or of loss involves the establishment of a present right to income or a present liability for expenditure. If the taxpayer was

on, an accrual basis, there could have been no accrual in 1916, since there was then no unconditional right to receive the proceeds of the oil sales. The fact that the taxpayer had entered the amount on its books for 1916 is not conclusive.

During the receivership the petitioner had no more than a claim to the receipts from the land; it did not as in 1917 and thereafter have the receipts themselves as its absolute property which it was free to use as it chose, being itself subject only to a claim of the Government. The determination in 1917 of petitioner's present right to receive the impounded fund constituted an accrual of income just as the determination of the taxpayer's obligation to pay constituted an accrual of loss in *Lucas* v. *American Code Co.*, 280 U. S. 445.

Nor should the reporting of the income be deferred until the year 1922 when the litigation was finally settled. There is little to distinguish the position of a taxpayer on the accrual basis who has earned and collected income but whose right to the income is being disputed and the position of a taxpayer on the cash basis similarly situated.

The petitioner is not excused from reporting income received in 1917 (and in later years as well) because it may later be required to respond to a claim the validity of which is wholly uncertain. The possibility that the taxpayer might have to repay the amount to the Government was a mere contingency which did not prevent the accrual of income.

ARGUMENT

I

THE RECEIVER WAS NOT REQUIRED TO FILE AN INCOME-TAX RETURN FOR 1916 IN BEHALF OF THE PETITIONER AND TO REPORT THEREIN INCOME IMPOUNDED BY HIM DURING THAT YEAR

The first issue raised is whether the receiver should have reported the sum of $171,979.22, derived during 1916 from the sale of oil produced on a parcel of land in Kern County, California, which may conveniently be referred to as Section 2.

The receiver was appointed to take possession only of Section 2 and to impound the receipts arising therefrom. The petitioner owned considerable other property and operated many wells in addition to those on Section 2. (R. 92–110.)

The court below, distinguishing between a situation of this kind and one where the receiver is in charge of the entire business or property of the corporation and is acting for it, held that one who is receiver for only a part of the property of a corporation is not required to file a return or pay a tax in respect of the impounded receipts. We submit that this was a correct conclusion under the law and the regulations.

Section 10 of the Revenue Act of 1916, *infra*, imposes a tax upon "the total net income received in the preceding calendar year from all sources by every corporation." Under Section 13 (a), *infra*, every corporation is required to render returns of such income.

Section 13 (c) of the Revenue Act of 1916 provides as follows:

> In cases wherein receivers, trustees in bankruptcy, or assignees are operating the property or business of corporations, joint-stock companies or associations, or insurance companies, subject to tax imposed by this title, such receivers, trustees, or assignees shall make returns of net income as and for such corporations, joint-stock companies or associations, and insurance companies, in the same manner and form as such organizations are hereinbefore required to make returns, and any income tax due on the basis of such returns made by receivers, trustees, or assignees shall be assessed and collected in the same manner as if assessed directly against the organizations of whose businesses or properties they have custody and control.

This provision was left unchanged by the amendments of the Revenue Act of 1916 made by the Revenue Act of 1917, and was thus in effect for both in 1916 and 1917.

The above statute refers to receivers and others who "are operating the property or business of corporations * * *." The use of the definite article "the" in this phrase is some indication that it is only where the receiver is in charge of *all* the property or business of a corporation that he is required to make a return of income in behalf of the corporation. This interpretation is fortified by the fact that the receiver is required to make returns of net in-

come "as and for such corporations" and the tax due thereon is to be assessed and collected "in the same manner as if assessed directly against the organizations of whose businesses or properties they have custody and control." This language could not have been used if it had been intended that the corporation should file a return in respect of income not falling within the receivership and the receiver another return for the same year of the income of which he had control. On the contrary, the language contemplates a substitution of the receiver for the corporation, and that can occur only when the receiver is in complete charge of all of the property or business of a corporation. Cf. *Reinecke* v. *Gardner*, 277 U. S. 239, involving Section 13 (c) of the Revenue Act of 1916 where the court said (p. 241):

> As under the bankruptcy act the entire property of the bankrupt vested in the trustee, the income in question was not the income of the bankrupt corporation, but of the trustee and was subject to income and excess-profits tax only if the statutes authorized the assessment of the tax against him. * * *

The regulations of the Treasury Department have consistently construed the statutes regarding receivers as applying only to receivers in charge of the entire property or business of a corporation and in all other cases have required corporations themselves to report their income.

Article 26 of Regulations 33, revised, (Revenue Acts of 1916 and 1917), *infra*, p. 38, indicates that it is only a receiver acting in the stead of his principal who is required to file a return and Article 209, *infra*, p. 38, provides as follows:

> Section 13, paragraph C, of this title requires receivers, trustees in bankruptcy, or assignees, who are in charge of and are operating the property and business of corporations, to make returns of annual net income and pay any income tax thereby shown to be due, regardless of what disposition, subject to the orders of the court, may be made of such income.
>
> Notwithstanding the fact that the powers and functions of the corporation are suspended and that the property and business are for the time in control and custody of the receiver, trustee, or assignee, subject to the orders of the court, such receiver, trustee, or assignee stands in the place of the corporate officers and is required for the purpose of this title to perform all the duties and assume all the liabilities which would devolve upon the officers of the corporation were they in control. The income which he receives on account of the business transacted is the income of the corporation and, no matter how such income is applied, it is subject to the tax imposed by this title in so far as it exceeds the deductions or allowances authorized by law.
>
> The receiver, trustee, or assignee acting for the corporation is required to make a

> true and accurate return of annual net income covering each year or part of each year during which he is in custody and control of the business or properties and will be liable to all the penalties imposed by this title for failure to meet any of its requirements.

Articles 424 and 622 of Regulations 45 (Revenue Act of 1918), *infra,* embody the same rule in more specific language. Article 424 gives as an illustration of receivers not liable—"a receiver of the rents and profits appointed to hold and operate a mortgaged parcel of real estate, but not in control of all the property or business of the mortgagor," and also receivers in partition proceedings. Article 622 makes it clear, as does Article 209 of Regulations 33, *infra,* p. 38 that it is only in cases where the receiver or trustee is in complete control and the powers and functions of the corporation are for the time being suspended that a receiver or trustee is required to file a return.

It is true that Regulations 45 were promulgated under the Revenue Act of 1918 and Section 225 of that Act changed Section 8 (c) of the Revenue Act of 1916, so as to provide specifically that receivers in possession of only a part of the property of an *individual* need not file a return; but Section 239 of the Revenue Act of 1918, *infra* p. 36, made no corresponding change as to receivers of corporations. Yet the Treasury Department continued to make the same regulations for both individuals and cor-

porations and did not change them in substance from what they had been under the Revenue Act of 1916.

To the same effect are Articles 424 and 622 of Regulations 62, 65, and 69, and Article 392 of Regulations 74 (Revenue Acts of 1921, 1924, 1926, and 1928, respectively).

This settled administrative construction of similar statutory provisions relating to the filing of returns by receivers and trustees in bankruptcy of corporations is entitled to great weight. *Brewster* v. *Gage*, 280 U. S. 327; *National Lead Co.* v. *United States*, 252 U. S. 140. The administrative interpretation has also received legislative approval, since Congress during the period that the regulations were in effect repeatedly enacted provisions as to receivers[2] which in so far as corporations were concerned were identical in all material respects with Section 13 (c) of the Revenue Act of 1916. *Brewster* v. *Gage*, *supra*.

If the departmental construction of Section 13 (c) of the Revenue Act of 1916 had been deemed incorrect, Congress would no doubt have changed the law in the revisions of 1918, 1921, 1924, or 1926. See *Heiner* v. *Colonial Trust Co.*, 275 U. S. 232.

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[2] See Section 239 of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1081; Section 239 (a) of the Revenue Act of 1921, c. 136, 42 Stat. 227, 259; Section 239 (a) of the Revenue Act of 1924, c. 234, 43 Stat. 253, 287 (U. S. C., Title 26, Section 991); Section 239 (a) of the Revenue Act of 1926, c. 27, 44 Stat. 9, 45 (U. S. C. App., Title 26, Section 991).

The regulations achieve a reasonable result since there is no provision in the acts for the consolidation of the return of the receiver of part of a corporation's property or business and the return of the corporation itself. It would obviously be unreasonable to require the filing of two separate returns for the same year, each covering only a part of the corporate income without provision for consolidation so that the tax could be based upon the income as a whole.

The case of *Forstmann* v. *Ferguson*, 17 F. (2d) 659 (N. J.), affirmed, 25 F. (2d) 47 (C. C. A. 3d), relied on by petitioner, did not involve any question as to the liability of a receiver for filing returns. The case concerned the taxation of certain dividends declared in 1919 and 1920 upon stock which the Alien Property Custodian had seized as enemy property under the Trading with the Enemy Act of October 6, 1917, c. 106, 40 Stat. 411. In connection with litigation relative to the shares, the court restrained the corporation from paying dividends on the stock in question and the owner from transferring the stock. It was held in that case that, as the corporation was required to hold the dividends under the restraining order, a trust existed and the income was taxable to the corporation as trustee for the years 1918 and 1919 under Sections 219 and 225 of the Revenue Act of 1918, and was not taxable to the owner.

The return that is filed by a receiver or a trustee in bankruptcy in behalf of a corporation is not a

fiduciary return within the meaning of the sections of the 1918 Act considered in the *Forstmann* case. See Article 422 of Regulations 45, *supra*. Nor would it have been under the Revenue Act of 1916. Cf. Sections 8 (c) and 13 (c), *infra*, p. 35. The tax on a fiduciary return is computed as that of an individual (see Section 219) whereas the return filed by a receiver or a trustee in bankruptcy of a corporation under Section 13 (c) of the Revenue Act of 1916 or under Section 239 of the Revenue Act of 1918 is a corporate return. *Reinecke* v. *Gardner*, *supra;* Article 209 of Regulations 33; Article 424 of Regulations 45. The *Forstmann* case seems to have no bearing on the present problem.

The case of *Hart* v. *Commissioner*, 54 F. (2d) 848 (C. C. A. 1st), is somewhat similar to the *Forstmann* case. In that case in a proceeding ancillary to a receivership a receiver of a corporation had secured a judgment against an individual in a state court in a large sum, and instead of requiring a bond to be filed upon appeal that court, upon petition of the defendant for an order segregating his assets, ordered him to turn over to the receiver for the corporation Liberty bonds equal in value to his entire assets. Interest on these bonds was collected by the receiver for the corporation in 1926 and the question was whether it was taxable to him or to the individual. The court held that in so far as the bonds were concerned the receiver for the corporation was in the

position of a trustee holding property for the benefit of an unascertained person and was required to file a return and pay the tax upon the interest, the individual not being taxable.

We submit that under the circumstances of this case there was no duty upon the receiver to file a return, and we pass to a consideration of the year for which the income should be taxed to the petitioner, which received it in 1917.

II

THE RECEIPTS IMPOUNDED IN 1916 AND RELEASED AND PAID OVER TO THE PETITIONER IN 1917 ARE TAXABLE TO THE PETITIONER FOR THE YEAR 1917 WHEN RELEASED AND NOT FOR 1916 WHEN IMPOUNDED, OR FOR 1922 WHEN THE DECREE UNDER WHICH THEY WERE RELEASED WAS AFFIRMED ON APPEAL

The Board of Tax Appeals made no finding as to whether the taxpayer filed its returns on the cash receipts and disbursements basis or on the accrual basis, although the Commissioner asserted that the former was true (R. 139), but held that the fact was immaterial, since the receiver was required to report the impounded income. In his petition for review by the Circuit Court of Appeals, the Commissioner asserted that the taxpayer was on the cash receipts and disbursements basis during the years in question (R. 148), and assigned as error the holding of the Board of Tax Appeals that it was immaterial whether taxpayer's accounts were kept on that basis. (R. 150.) The court below did not pass upon the question but reversed the Board,

holding that under either system of accounting the income was taxable for 1917.

Although the record is not wholly free from doubt, we think that the Board should have found that the returns were filed on a cash basis. The returns for 1916 and 1917 contained a statement to the effect that they were filed on the cash basis. (R. 169, 178.) While this statement is not conclusive (*Aluminum Castings Co. v. Routzahn*, 282 U. S. 92, 99), it is entitled to considerable weight, particularly since the returns show that no inventories were taken and there is nothing in them to contradict the statement that they were filed on the cash basis.

The taxpayer introduced no evidence as to the basis upon which the returns were filed and the only things in the record which might be taken to indicate an accrual basis are certain statements in the deficiency letter for 1917 to the effect that the Commissioner had disallowed taxes paid in excess of accruals. (R. 23, 24.) We think the statement is susceptible of more than one meaning. It might mean that taxes had been paid before they became due and were not considered a proper charge for that year.[8]

[8] The deficiency letter for 1918 and 1919 (the appeal in that case having been consolidated with the instant case before the Board) recites that interest receivable accrued had been disallowed in accordance with Article 87 of Regulations 45. (R. 68.) The references to accruals in the 1918 and 1919 deficiency letter have no real bearing on this question but in any event they are not clear since the same letter refers to the allowance of a deduction of taxes paid. (R. 69.)

The petitioner argues that the question of the taxability of the impounded income for 1917 was not raised in the original deficiency letter but in a claim for an increased deficiency and hence that the burden of proof as to the basis of filing the returns rested upon the Commissioner.

It is our position that the presumption of correctness of the Commissioner's determination attaches to the increased deficiency as well as to the original deficiency and that the Board's rules so far as they provide otherwise should be disregarded as not in accordance with the law; but (assuming that a cash basis is essential to sustain the tax) even if the burden of proof were on the Commissioner that burden has been sustained. This argument is developed more at length in Appendix B of the brief, *infra*, p. 41.

But we submit that the court below correctly decided that irrespective of the basis of filing the returns the income was taxable for 1917 and proceed to deal with the case under both the cash and the accrual theory.

(a) *If the taxpayer was on the cash basis the income was taxable for 1917, when it was actually received, and not for 1916 or 1922*

The petitioner argues that if the income was not taxable to the receiver for 1916 it was taxable to the corporation either for 1916 when the income was produced or in the alternative for the year 1922 when the Government's claim to it was finally determined to be invalid.

We understand the petitioner's contention that the income was taxable for 1916 to be based entirely on the assumption that the return was filed on the accrual basis and that it does not deny that the income would be taxable for 1917 if the return was on the cash basis. If, however, we are in error as to a concession being made, we submit that any other position is wholly without support.

The theory of a cash receipts and disbursements method of accounting is that from income actually received in cash or its equivalent during the taxable year there are deducted expenses actually paid. *United States* v. *Anderson*, 269 U. S. 422; *United States* v. *Mitchell*, 271 U. S. 9; *Eckert* v. *Burnet*, 283 U. S. 140; *Aluminum Castings Co.* v. *Routzahn*, 282 U. S. 92; *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359.

There was no physical receipt of the impounded income in 1916. There was such receipt in 1917 when the impounded funds were released to and received by the taxpayer. Under the cash basis of accounting the amount was taxable for 1917, the year of its receipt.

Clearly, the amount could not be taxed as an amount received during 1916, even if it had been known at that time that payment would be made in 1917, which was not the case. In *Maryland Casualty Co.* v. *United States*, 251 U. S. 342, this Court distinguished between the actual receipt of cash and money to be received in the future; and in *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, the

Court held that a taxpayer on the cash basis should be required to report damages recovered as income for the year in which the judgment was paid and not for earlier years in which amounts were expended in the attempted performance of the contract there involved.

Under those decisions we submit that the impounded income was received in 1917 and was taxable for that year.

The petitioner apparently does not invoke the doctrine that one may be taxed upon income which he has constructively, if not actually, received, and we have found no phase of that doctrine which will fit the instant case.[4] There is nothing in that

[4] The most generally applied rule of constructive receipt is that a taxpayer may be taxed upon income not yet received when the amount has been unqualifiedly made subject to his demand during the taxable year and its receipt or nonreceipt is a matter within his own control. *Commissioner* v. *Bingham* (C. C. A. 6th), 35 F. (2d) 503, certiorari denied, 281 U. S. 729; *Hadley* v. *Commissioner* (App. D. C.), 36 F. (2d) 543; *Brooks* v. *Commissioner* (C. C. A. 4th), 35 F. (2d) 178; *Schoenheit* v. *Lucas* (C. C. A. 4th), 44 F. (2d) 476. Cf. *Commissioner* v. *Adams* (C. C. A. 1st), 54 F. (2d) 228. In the instant case the order appointing the receiver had destroyed the power of the corporation to collect the income and it had no right to demand payment from the receiver.

The instant case is not within the rule of *Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716, and *United States* v. *Boston & M. R. Co.*, 279 U. S. 732, in which it is recognized that one may receive taxable income through the payment of his obligation by another.

Nor is it within the rule of decisions recognizing that a person may be taxed upon income of which he is not the ultimate beneficial owner when he has voluntarily deprived

theory which requires a taxpayer to report income which it may never receive. *Burnet* v. *Logan*, 283 U. S. 404.

Nor is the case taken outside the rule that a taxpayer on the cash basis must report income for the year in which it is actually received by the fact that the Government was claiming the income in 1917, and continued to claim it until the litigation was finally terminated in 1922. We submit that a taxpayer who has received payment under a claim of right and without restriction as to his disposition of it has received income which he is required to report, even though others may claim that he is not entitled to the payment and is accountable to them.

To hold otherwise would do violence to the principle that the income tax is one imposed for an annual period; that it takes into consideration yearly gains and losses. *Burnet* v. *Thompson Oil & Gas Co.*, 283 U. S. 301; *Burnet* v. *Sanford & Brooks Co., supra; De Loss* v. *Commissioner*, 28 F. (2d) 803 (C. C. A. 2d).

That a taxpayer on the cash basis may not defer reporting income actually received under a claim of right on the ground that claims are being asserted the outcome of which may later deprive him of it, was decided in *Board* v. *Commissioner*, 51 F. (2d)

himself of such ownership by an independent agreement or deed. *Leininger* v. *Commissioner*, No. 426, decided March 14, 1932; *Lucas* v. *Earl*, 281 U. S. 111; *Mitchel* v. *Bowers* (C. C. A. 2d), 15 F. (2d) 287, certiorari denied, 273 U. S. 759.

73 (C C. A. 6th), certiorari denied, 284 U. S. xv. In that case corporation A sold all of its assets and went into liquidation. At that time A had entered into a contract for the construction of a pipe line. The other party to the contract was unable to finance his part of the agreement. It was taken over by the liquidating trustees and two other officers and the pipe line was constructed on the joint credit of A and the five officers. Upon the sale of the properties of A, the liquidating trustees distributed a part of the proceeds to the taxpayer and other liquidating trustees in 1920. Certain stockholders contested this distribution and filed an action which was not finally settled until 1927. In holding that the taxpayer was required to report the amount as income for 1920 rather than for 1927, the court said (pp. 75–76):

> We are of the opinion that the board was right in allocating this income to the year 1920. That it was actually received during that year is not disputed; nor is it disputed that it was received under a claim of right and as profits to which the petitioner was justly entitled. The only claim made is that the contract whereby petitioner purported to secure his interest in the pipe line was illegal and unenforceable by reason of his position as a director of the Old Dominion Oil Company. In this contention the petitioner of course never acquiesced. The payment was never refunded. Possibly it might have been recovered in the litigation which

> was instituted for that purpose, but it was not, and it is at least unusual that a taxpayer should be heard to assert the possibility of an adjudication of alleged misconduct and breach of trust, as relieving him from tax liability which is predicated upon the assumption of the honesty and legality of his acts. Obviously, the sum involved must be considered as income either for the year 1920 or 1927, and we think that it must be allocated to the year 1920, in which it was actually received, rather than to the year 1927, in which the taxpayer's right to retain it was established.

The situation in the present case is very similar to that in the *Board* case and the same principle should apply. These two cases present a corollary to the rule in *Burnet* v. *Sanford & Brooks Co., supra.*

In that case the taxpayer brought an action against the Government for damages, alleging that the Government had failed to make a proper disclosure as to the character of the material which the taxpayer contracted to dredge. The judgment was not recovered and paid until 1920, and the Court held that the amount paid on the judgment was taxable for that year and not for the earlier years. The difference between that case and the case at bar is that there the taxpayer in the earlier years was claiming a right to income which it had not received, whereas here the taxpayer during the earlier year was not only asserting its claim to the income but had actually collected it.

If in this case the taxpayer had finally lost its appeal and been obliged to account for the profits, it would have been entitled to a deduction for a loss in that year, but the obligation of reporting the income actually realized in 1917 was not affected by the fact that a loss might be sustained in the future.

This is analogous to the rule that limitations which may affect the right to dispose of income do not prevent it from being taxed when received. *Cleveland Ry. Co.*, v. *Commissioner*, 36 F. (2d) 347 (C. C. A. 6th), certiorari denied, 281 U. S. 743; *Newman* v. *Commissioner*, 40 F. (2d) 225 (C. C. A. 10th), certiorari denied, 282 U. S. 858; *Rodrigues* v. *Edwards*, 40 F. (2d) 408 (C. C. A. 2d).

(*b*) *Assuming for the sake of argument that the taxpayer was on the accrual basis, the impounded receipts were nevertheless taxable for 1917 and not for 1916 or 1922*

The petitioner's argument that the impounded receipts represented accrued income for 1916 rather than 1917 is apparently based on two contentions: (1) that the income was entered on the books of the corporation as earned or accrued income during 1916, and (2) that the test of the accrual of income is not whether the taxpayer has the present beneficial use of or right to the income but whether the right to it is ultimately established. It claims that the effect of the decision in *United States* v. *North American Oil Consolidated*, 264 Fed. 336 (C. C. A. 9th), is that at all times the petitioner was entitled to the possession of Section 2 and to the income

realized therefrom and hence that it had a right to such income in 1916 and should be taxed upon it for that year.

Section 13 (d) of the Revenue Act of 1916, *supra*, permits a taxpayer to file a return in accordance with the method of accounting employed in keeping its books, provided the method employed clearly reflects income. This does not mean, however, that the fact that an item has been entered on the books as an accrual in a particular year conclusively shows that it was properly accrued in that year or that the Commissioner may not correct an item improperly accrued. *United States* v. *American Can Co.*, 280 U. S. 412; *Aluminum Castings Co.* v. *Routzahn*, 282 U. S. 92.

The general rule is that income may be said to have accrued when it is earned (*United States* v. *Anderson*, 269 U. S. 422), and, in the case of income derived from the sale of property, income may be said to have accrued to the vendor when the vendee's obligation to pay has become unconditional. *United States* v. *American Can Co., supra; Lucas* v. *North Texas Co.*, 281 U. S. 11; *Evergreen Cemetery Ass'n* v. *Burnet*, 45 F. (2d) 667 (App. D. C.); *Rouss* v. *Bowers*, 30 F. (2d) 628 (C. C. A. 2d), certiorari denied, 279 U. S. 853.

While the source of the income here involved was the production and sale of oil in 1916, the petitioner first acquired the right to be paid the proceeds of the sales in 1917 when the receiver was discharged and the impounded funds released. (R. 120.)

Thus, while an unconditional liability on the part of purchasers to pay for the oil existed prior to 1917, there was no corresponding right in the petitioner to collect. The property was in *custodia legis* and neither claimant could assert dominion or control over the corpus of the estate or the income. The rights of both the parties were in suspension during the receivership. Hence the broad principles laid down in *Lucas* v. *North Texas Co., supra,* and other cases just cited have only a general application to this case and do not furnish a determinative rule.

The accrual of income or of loss involves a present right to income or a present liability for expenditure. Accrual occurs only when gain or loss is realized, or where the right or the liability can be established and is ascertainable with reasonable certainty. *Lucas* v. *American Code Co., supra,* p. 449. In this case the amount of the 1916 receipts which the petitioner would acquire upon the dissolution of the receivership may have been ascertainable in that year; but whether the petitioner would then, or ever, acquire them was not certain in 1916 and could not in that year be established to a reasonable degree of certainty, or indeed to any degree of certainty.

With respect to whether the income in question accrued in 1916 or 1917, this case closely resembles, in principle, the case of *Lucas* v. *American Code Co., supra.* There it was held that the taxpayer could not, during the period intervening between

the breach of a contract and the final adjudication of its liability therefor, deduct in the form of an annual reserve the damages which it estimated might be payable. There existed only a claim; neither liability nor amount was presently ascertainable. So in this case, petitioner had during the period of receivership nothing more than a claim to the receipts from the land; it did not, as was the case in 1917 and thereafter, have actual dominion over the receipts as its absolute property, the petitioner itself then being subject only to a claim of the Government which might or might not be established. And the validity of petitioner's claim to the receipts during receivership must be said to have been uncertain and unascertainable by reason of the fact that in the deliberate judgment of a Federal district court it was so uncertain as to require the court, for the protection of the interest of the adverse claimant, to take from the petitioner the benefit of those receipts and place the receipts themselves in *custodia legis* pending its own determination of the controversy as to who should receive them. The fact that in 1917 the petitioner was held to be entitled to, and did, receive them can not be given retrospective effect for the purpose of determining *in 1916* that the impounded receipts accrued to the petitioner as income for that year. The determination, in 1917, of petitioner's present right to *receive* the impounded fund constituted an accrual of income in this case, just as the determina-

tion of the taxpayer's obligation to *pay* constituted an accrual of loss in the *American Code* case. See also *Pharr & Sons, Ltd.* v. *Commissioner* (C. C. A. 5th) net yet reported, decided March 19, 1932.

The conclusion of the court below that the income was not accrued in 1916 is in accord with the decision in *Corn Exchange Bank* v. *United States,* 37 F. (2d) 34 (C. C. A. 2d), where it was held that a taxpayer is not obliged to report interest which it has entered on its books as an accrued item where at the end of the year the debtor was in the hands of a receiver and the probabilities were that the interest would not be collected. In this case, where the receipt of the income depended not upon the condition of the debtor but upon the outcome of pending litigation, there seems to be stronger reason for not accruing the income in 1916.

See also *Becker Bros.* v. *United States,* 7 F. (2d) 3 (C. C. A. 2d); *Malleable Iron Range Co.* v. *United States,* 62 C. Cls. 425, 273 U. S. 674, 65 C. Cls. 441; *Commissioner* v. *Southeastern Express Co.* (C. C. A. 5th), decided March 4, 1932, not yet reported.

The decision in *Obispo Oil Co.* v. *Welch,* 48 F. (2d) 872 (S. D. Cal.), is *contra* and is now pending before the same Circuit Court of Appeals that decided the instant case. The facts in that case were the same as in this, except that the corporation had originally reported the income for the years in which the oil was produced notwithstanding the receivership, and the litigation was terminated by

a settlement in 1920. The District Court held the income to be taxable for the earlier years.[5]

We have heretofore discussed the question of accrual in 1917 as against accrual in 1916. The petitioner, in an alternative argument, urges that if the income was not taxable for 1916 it was not subject to tax until 1922 when the litigation with the Government was finally terminated. It relies upon *Consolidated Tea Co.* v. *Bowers,* 19 F. (2d) 382 (S. D. N. Y.).

As previously pointed out, in *Board* v. *Commissioner,* 51 F. (2) 73 (C. C. A. 6th), certiorari denied, 284 U. S. xv, it was recognized that a taxpayer on the cash basis may not refuse to report income actually received under a claim of right on the ground that claims are being asserted which may later deprive him of it. There seems to be little difference between the position of the taxpayer in that case and the position of a taxpayer on the accrual

[5] The Court's attention should be called to the case of *Commissioner* v. *Old Dominion S. S. Co.*, 47 F. (2d) 148 (C. C. A. 2d), where the court held that there should be taxed to a carrier as accrued income during the period of Federal control not only the compensation representing the standard return, but also the excess allowed over the standard return although the amount of the excess was not determined until a later year. We think that decision, whether right or wrong, is distinguishable on the facts. The same question is now before the Circuit Court of Appeals for the Tenth Circuit in the case of *Commissioner* v. *Midland Valley Railroad Co.* (see 19 B. T. A. 423). See also *Kentucky & Indiana Terminal Railroad Co.* v. *Commissioner*, 54 F. (2d) 738 (C. C. A. 6th), petition for certiorari filed, No. 817, October Term, 1931.

basis who has earned and collected income and holds it as free assets but whose right to it is being disputed. The reasoning of the court in that case supports the decision here.

The case of *United States* v. *White Dental Co.*, 274 U. S. 398, is also applicable, whether the taxpayer is on the cash or the accrual basis. If under that decision a taxpayer is not compelled to defer a deduction for a loss realized with respect to a German-owned subsidiary during the World War until it should be ascertained that there was no possibility of a recovery by an award of the Mixed Claims Commission, by a parity of reasoning the taxpayer in this case should not be permitted to defer reporting income actually received because of the possibility that it may later have to pay a corresponding amount to the Government. The termination of the litigation in 1922 gave the taxpayer nothing that it did not already have; it merely relieved petitioner of the possibility of being required to account to and compensate the United States for a wrongful occupancy and use of the land. In the *White* case taxpayer was not precluded from deducting the value of property lost, because he owned a claim the enforceability of which was uncertain. In this case petitioner is not excused from reporting income received in 1917 (and in the later years as well), because it may later be required to respond to a claim the validity of which is wholly uncertain.

On this aspect of the case our position that the income was accrued prior to the termination of the litigation is contrary to the decision in *Commissioner* v. *Brown,* 54 F. (2d) 563, (C. C. A. 1st) (pending on petition for certiorari by the Commissioner, October Term, 1931, No. 776, petition for certiorari also filed by taxpayer, No. 797.) In that case a partnership transacted its wool business during 1918 and 1919 under a permit issued by the War Industries Board. The regulations of the Board provided *inter alia* that the Government should have a prior right to acquire all of the 1918 wool clip at prices to be officially fixed plus certain compensation for distribution charges and that if at the end of the season the gross profits (including the commission) were found to be in excess of 5% the excess profits should be disposed of as the Government should subsequently direct. The partnership refused to give up the excess profits for distribution to the growers as the Government demanded and was sued by the Government, the litigation terminating in the partnership's favor in 1930. It was held that the income was taxable for 1930. The court in that case in substance decided that a taxpayer on the accrual basis may not be taxed upon income which he has earned and collected while claims are being asserted against him on account of it or litigation is pending which may deprive him of it. We think the decision wrong.

The decision in the *Consolidated Tea Company* case, *supra,* relied upon by petitioner is not opposed

to the decision in this case. The sole question there was whether the taxpayer could in 1919 deduct as a loss a judgment rendered against it by a lower court in 1919 and affirmed by the appellate court in 1921 and paid in 1921. That case might have some resemblance to the case at bar if the judgment had actually been paid in 1919, but as it stands it is not authority for the proposition that a corporation, which has collected money as a part of its income and used it in its business as it would any other funds, may refrain from reporting the income because its right to retain the amount is being litigated. Cf. *Lucas* v. *American Code Co., supra.*

In *Vang* v. *Lewellyn,* 35 F. (2d) 283 (C. C. A. 3d), the court held, in substance, that a road contractor could not refuse to accrue income realized under a contract until the end of a five-year period on the ground that it had obligated itself to maintain the road during that period. The court pointed out that the liability for maintenance was contingent upon the need for maintenance and that gain or loss on the contract was realized when the contract was completed, notwithstanding the possibility that expenses might thereafter be incurred. See also the decision of the lower court in the same case, *Harrison* v. *Heiner,* 28 F. (2d) 985 (W. D. Pa.).

In this case also, the termination of the litigation in 1922 might have had some bearing upon petitioner's right to a deduction in that year had it not prevailed, but it did not serve to prevent the accrual of income in 1917.

CONCLUSION

The Circuit Court of Appeals properly held that the receiver was not required to file a return with respect to the impounded receipts and that the petitioner was taxable thereon as income for the year 1917.

Respectfully submitted.

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APRIL, 1932.

APPENDIX A

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1916, c. 463, 39 Stat. 756, 765, 767, 770, 771:

SEC. 10. That there shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources by every corporation, joint-stock company or association, or insurance company, organized in the United States, no matter how created or organized but not including partnerships, a tax of two per centum upon such income; * * *

SEC. 12. (a) In the case of a corporation, joint-stock company or association, or insurance company, organized in the United States, such net income shall be ascertained by deducting from the gross amount of its income received within the year from all sources—

* * * * *

SEC. 13. (a) The tax shall be computed upon the net income, as thus ascertained, received within each preceding calendar year ending December thirty-first;

* * * * *

(c) In cases wherein receivers, trustees in bankruptcy, or assignees are operating the property or business of corporations, joint-stock companies or associations, or insurance companies, subject to tax imposed by this

title, such receivers, trustees, or assignees shall make returns of net income as and for such corporations, joint-stock companies or associations, and insurance companies, in the same manner and form as such organizations are hereinbefore required to make returns, and any income tax due on the basis of such returns made by receivers, trustees, or assignees shall be assessed and collected in the same manner as if assessed directly against the organizations of whose businesses or properties they have custody and control; * * *

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1074, 1081:

SEC. 225. That every fiduciary (except receivers appointed by authority of law in possession of part only of the property of an individual) shall make under oath a return for the individual, estate or trust for which he acts (1) if the net income of such individual is $1,000 or over if single or if married and not living with husband or wife, or $2,000 or over if married and living with husband or wife, or (2) if the net income of such estate or trust is $1,000 or over or if any beneficiary or such estate or trust is a nonresident alien, stating specifically the items of the gross income and the deductions and credits allowed by this title. Under such regulations as the Commissioner with the approval of the Secretary may prescribe, a return made by one of two or more joint fiduciaries and filed in the office of the collector of the district where such fiduciary resides shall be a sufficient compliance with the above requirement. The fiduciary shall make oath that he has sufficient knowledge of the affairs of such individual, estate or trust to enable him to make the return, and

that the same is, to the best of his knowledge and belief, true and correct.

* * * * *

SEC. 239. That every corporation subject to taxation under this title and every personal service corporation shall make a return, stating specifically the items of its gross income and the deductions and credits allowed by this title. The return shall be sworn to by the president, vice president, or other principal officer and by the treasurer or assistant treasurer. If any foreign corporation has no office or place of business in the United States but has an agent in the United States, the return shall be made by the agent. In cases where receivers, trustees in bankruptcy, or assignees are operating the property or business of corporations, such receivers, trustees, or assignees shall make returns for such corporations in the same manner and form as corporations are required to make returns. Any tax due on the basis of such returns made by receivers, trustees, or assignees shall be collected in the same manner as if collected from the corporations of whose business or property they have custody and control.

* * * * *

Revenue Act of 1926, c. 27, 44 Stat. 9, 56:

SEC. 274. (e) The Board shall have jurisdiction to redetermine the correct amount of the deficiency even if the amount so redetermined is greater than the amount of the deficiency, notice of which has been mailed to the taxpayer, and to determine whether any penalty, additional amount or addition to the tax should be assessed, if claim therefor is asserted by the Commissioner at or before the hearing or a rehearing. (U. S. C. Sup. V. Title 26, Sec. 1048(c).)

Treasury Regulations 33 (Revised):

Art. 26. * * *

RULINGS ON MAKING RETURNS

* * * * *

181. Receivers who, as officers of a court, stand in the stead of some principal are required to account for income tax as the principal would have been required to account.

* * * * *

ART. 209. *Receivers to make returns.*—Section 13, paragraph C, of this title requires receivers, trustees in bankruptcy, or assignees, who are in charge of and are operating the property and business of corporations, to make returns of annual net income and pay any income tax thereby shown to be due, regardless of what disposition, subject to the orders of the court, may be made of such income.

Notwithstanding the fact that the powers and functions of the corporation are suspended and that the property and business are for the time in control and custody of the receiver, trustee, or assignee, subject to the orders of the court, such receiver, trustee, or assignee stands in the place of the corporate officers and is required for the purpose of this title to perform all the duties and assume all the liabilities which would devolve upon the officers of the corporation were they in control. The income which he receives on account of the business transacted is the income of the corporation and, no matter how such income is applied, it is subject to the tax imposed by this title in so far as it exceeds the deductions or allowances authorized by law.

The receiver, trustee, or assignee acting for the corporation, is required to make a true and accurate return of annual net income covering each year or part of each year during which he is in custody and control of the business or properties and will be liable to all the penalties imposed by this title for failure to meet any of its requirements.

Treasury Regulations 45:

ART. 424. *Return by receiver.*—A receiver who stands in the stead of an individual or corporation must render a return of income and pay the tax for his trust, but a receiver of only part of the property of an individual or corporation need not. If the receiver acts for an individual the return shall be on form 1040 (revised) or 1040 A (revised). When acting for a corporation a receiver is not treated as a fiduciary, and in such a case the return shall be made as if by the corporation itself. See section 239 of the statute and article 622. A receiver in charge of the business of a partnership shall render a return on form 1065 (revised). A receiver of the rents and profits appointed to hold and operate a mortgaged parcel of real estate, but not in control of all the property or business of the mortgagor, and a receiver in partition proceedings, are not required to render returns of income. In general, statutory receivers and common-law receivers of all the property or business of an individual or poration must make returns. See also section 256 of the statute and articles 1071–1080.

ART. 622. *Returns by receivers.*—Receivers, trustees in dissolution, trustees in bankruptcy, and assignees, operating the property or business of corporations, must make returns of income for such corporations on

form 1120, covering each year or part of a year during which they are in control. Notwithstanding that the powers and functions of a corporation are suspended and that the property and business are for the time being in the custody of the receiver, trustee, or assignee, subject to the order of the court, such receiver, trustee, or assignee stands in the place of the corporate officers and is required to perform all the duties and assume all the liabilities which would devolve upon the officers of the corporation were they in control. A receiver in charge of only part of the property of a corporation, however, as a receiver in mortgage foreclosure proceedings involving merely a small portion of its property, need not make a return of income. See articles 424 and 547.

APPENDIX B

The petitioner argues that, since the tax which is the subject of controversy here was not a part of the original deficiency but was claimed as an increased deficiency in the answer of the Commissioner, the burden of proof was upon the Commissioner and he has failed to sustain that burden.

Rule 30 of the Board of Tax Appeals provides:

> BURDEN OF PROOF.—The burden of proof shall be upon the petitioner, except as otherwise provided by statute and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent.

We concede that the Board of Tax Appeals has consistently applied the last part of this rule to cases like the case at bar, where a taxpayer has taken an appeal to the Board in reference to certain matters and the Commissioner at or before the hearing or rehearing has asserted a claim for an increased deficiency based on other matters in accordance with Section 274 (e) of the Revenue Act of 1926, *infra*. It has construed the claim for increased deficiency as an affirmative pleading and has held that the burden of proof with respect to it is upon the Commissioner. *Henderson Tire & Rubber Co.*, 12 B. T. A. 716; *Schilling Grain Co.*, 8 B. T. A. 1048; *General Lead Batteries Co.*, 2 B. T. A. 392; *Crider Brothers Commission Co.*, 10 B. T. A. 338, affirmed on other grounds, 45 F. (2d) 974, certiorari denied, 283 U. S. 834. This applica-

tion of its rule appears to be based on the theory that the original deficiency notice carries with it a presumption of the correctness of the Commissioner's determination, and that the increased deficiency which necessarily challenges the correctness of the first determination can not also be treated as being presumptively correct. See *Georgiana McFetridge*, 9 B. T. A. 759; *Rines Real Estate Co.*, 12 B. T. A. 1370. In the *Schilling Grain Company* case, the Board said (pp. 1057–1058):

> The burden of proving this allegation is upon the respondent and unless it is shown by a preponderance of the evidence that his allowance (that is, the original deficiency letter) was erroneous, we would not be justified in changing his previous action. * * *

Whether the Board is justified in holding that the burden of proof rests upon the Commissioner in cases like the *Schilling Grain Company* case and the case at bar has not been passed upon by any court. It seems to conflict with the rule generally recognized in proceedings before the Board as well as in suits to recover a tax already paid that the Commissioner's determination is *prima facie* correct or presumptively correct and that in all such proceedings the burden of proving the Commissioner wrong is upon the taxpayer. *Niles Bement Pond Co.* v. *United States*, 281 U. S. 357; *Wickwire* v. *Reinecke*, 275 U. S. 101; *Reinecke* v. *Spalding*, 280 U. S. 227; *United States* v. *Mitchell*, 271 U. S. 9; *Lucas* v. *Kansas City Structural Steel Co.*, 281 U. S. 264; *Burnet* v. *Houston*, 283 U. S. 223.

There seems to be no reason for applying a different rule when the determination of the Commissioner is represented in an increased deficiency. Section 274 (e) of the Revenue Act of 1926 gives

authority to the Commissioner to assert an increased deficiency at or before a hearing or rehearing. See also *Cement Gun Co.* v. *Commissioner* (App. D. C.), 36 F. (2d) 107; *Moise* v. *Burnet*, 52 F. (2d) 1071 (C. C. A. 9th). The power of the Commissioner to redetermine a tax was conceded by this Court in *Burnet* v. *Porter*, 283 U. S. 230. The reason for presuming the correctness of the original assertion of the Commissioner applies with equal force to this supplemental assertion, and it would seem that in a case of this sort the second determination should be considered a correction of the first and the two considered together as a single determination to which the presumption of correctness attaches.

This conclusion is supported by the case of *Austin Co.* v. *Commissioner*, 35 F. (2d) 910 (C. C. A. 6th), certiorari denied, 281 U. S. 735. In that case the Commissioner had allowed a refund of 1917 taxes based on the taxpayer's claim for special assessment. Later, while the Revenue Act of 1924 was in effect, the Commissioner asserted a deficiency in tax and the taxpayer appealed to the Board. The court after distinguishing the case of *Woodworth* v. *Kales*, 26 F. (2d) 178 (C. C. A. 6th), in which it had held that the Commissioner could not reverse a previous determination, on the ground that in the *Woodworth* case it affirmatively appeared that the new action of the Commissioner was not based upon any fraud or mistake of law or fact but upon a changed inference of fact from the same evidentiary facts, said (p. 912):

> It is settled by the decisions of the Supreme Court that the findings of the com-

missioner are prima facie correct, and that the taxpayer who complains of them has the burden before the Board of Tax Appeals of showing that they are wrong. *Wickwire* v. *Reinecke,* 275 U. S. 101. It is said, however, that the presumption which arose from the fact of this additional assessment was overcome by a like presumption attaching to the original assessment, and that the burden was on the commissioner to show that his later action was taken for reasons authorized in the Woodworth Case. We can not concur in that view. The question before the Board concerned the additional assessment, not the earlier one. The action of the commissioner in making it was under attack. The law gave him the right to make it under certain circumstances. There is a presumption that he performed his duty, that is, that he acted upon all the facts before him, including new and different ones. *United States* v. *Chemical Foundation,* 272 U. S. 1. This presumption of the existence of such new facts is not inconsistent with the presumption attaching to the first assessment, that the commissioner acted upon all the facts then before him. Moreover, it was within the power of the petitioner to obtain the facts of both assessments through the processes of the Board of Tax Appeals. *Blair* v. *Oesterlein Machine Co.,* 275 U. S. 220. It did not do this, but relied upon lack of authority in the commissioner to make any further assessment. Even though there was lack of authority to make such assessment upon a changed view of the same facts, there was not lack of authority to make it where there was fraud or mistake of law or fact in the original assessment. In this situation the burden was on the petitioner to show that the com-

missioner's action grew out of circumstances which did not warrant it.

Cf. *Lewis* v. *Reynolds*, No. 115, October Term, 1931, decided January 4, 1932.

It is true that the appeal to the Board in the *Woodworth* case was taken under the Revenue Act of 1924 which contained no provision similar to Section 274 (e) of the Revenue Act of 1926, and that there was not an assertion of two deficiencies; but in that case as in this there were two determinations by the Commissioner and the question was whether the first or second determination of a Commissioner should control. The assertion of a deficiency by a sixty-day letter is essentially the same as and of no greater dignity than the assertion of it by the Commissioner's answer, and the reasoning in the *Austin* case applies here. See also *L. Loewry & Son* v. *Commissioner*, 31 F. (2d) 652 (C. C. A. 2d).

Even if the Board's rule should be sustained, we think the Commissioner sustained the burden of proof in this case by offering the return in evidence and that, the taxpayer having offered no evidence tending to contradict the statement on the return that they were made on a cash basis, the Board should have made a finding to that effect.

U. S. GOVERNMENT PRINTING OFFICE: 1932

SUPREME COURT OF THE UNITED STATES.

No. 575.—October Term, 1931.

North American Oil Consolidated, Petitioner,
vs.
David Burnet, Commissioner of Internal Revenue.

On Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit.

[May 23, 1932.]

Mr. Justice Brandeis delivered the opinion of the Court.

The question for decision is whether the sum of $171,979.22 received by the North American Oil Consolidated in 1917, was taxable to it as income of that year.

The money was paid to the company under the following circumstances. Among many properties operated by it in 1916 was a section of oil land, the legal title to which stood in the name of the United States. Prior to that year, the Government, claiming also the beneficial ownership, had instituted a suit to oust the company from possession; and on February 2, 1916, it secured the appointment of a receiver to operate the property, or supervise its operations, and to hold the net income thereof. The money paid to the company in 1917 represented the net profits which had been earned from that property in 1916 during the receivership. The money was paid to the receiver as earned. After entry by the District Court in 1917 of the final decree dismissing the bill, the money was paid, in that year, by the receiver to the company. *United States* v. *North American Oil Consolidated*, 242 Fed. 722. The Government took an appeal (without supersedeas) to the Circuit Court of Appeals. In 1920, that Court affirmed the decree. 264 Fed. 336. In 1922 a further appeal to this Court was dismissed by stipulation. 258 U. S. 633.

The income earned from the property in 1916 had been entered on the books of the company as its income. It had not been included in its original return of income for 1916; but it was included in an amended return for that year which was filed in

1918. Upon auditing the company's income and profits tax returns for 1917, the Commissioner of Internal Revenue determined a deficiency based on other items. The company appealed to the Board of Tax Appeals. There, in 1927 the Commissioner prayed that the deficiency already claimed should be increased so as to include a tax on the amount paid by the receiver to the company in 1917. The Board held that the profits were taxable to the receiver as income of 1916; and hence made no finding whether the company's accounts were kept on the cash receipts and disbursements basis or on the accrual basis. 12 B. T. A. 68. The Circuit Court of Appeals held that the profits were taxable to the company as income of 1917, regardless of whether the company's returns were made on the cash or on the accrual basis. 50 F. (2d) 752. This Court granted a writ of certiorari. 284 U. S. 614.

It is conceded that the net profits earned by the property during the receivership constituted income. The company contends that they should have been reported by the receiver for taxation in 1916; that if not returnable by him, they should have been returned by the company for 1916, because they constitute income of the company accrued in that year; and that if not taxable as income of the company for 1916, they were taxable to it as income for 1922, since the litigation was not finally terminated in its favor until 1922.

First. The income earned in 1916 and impounded by the receiver in that year was not taxable to him, because he was the receiver of only a part of the properties operated by the company. Under § 13 (c) of the Revenue Act of 1916,[1] receivers who "are operating the property or business of corporations" were obliged to make returns "of net income as and for such corporations", and "any income tax due" was to be "assessed and collected in the

[1] Act of September 8, 1916, 39 Stat. 756, 771, c. 463: "In cases wherein receivers, trustees in bankruptcy, or assignees are operating the property or business of corporations . . . , subject to tax imposed by this title, such receivers, trustees, or assignees shall make returns of net income as and for such corporations . . . , in the same manner and form as such organizations are hereinbefore required to make returns, and any income tax due on the basis of such returns made by receivers, trustees, or assignees shall be assessed and collected in the same manner as if assessed directly against the organizations of whose business or properties they have custody and control."

same manner as if assessed directly against the organization of whose business or properties they have custody and control." The phraseology of this section was adopted without change in the Revenue Act of 1918, 40 Stat. 1057, 1081, c. 18, § 239. The regulations of the Treasury Department have consistently construed these statutes as applying only to receivers in charge of the entire property or business of a corporation; and in all other cases have required the corporations themselves to report their income. Treas. Regs. 33, arts. 26, 209; Treas Regs. 45, arts. 424, 622 That construction is clearly correct. The language of the section contemplates a substitution of the receiver for the corporation; and there can be such substitution only when the receiver is in complete control of the properties and business of the corporation. Moreover, there is no provision for the consolidation of the return of a receiver of part of a corporation's property or business with the return of the corporation itself. It may not be assumed that Congress intended to require the filing of two separate returns for the same year, each covering only a part of the corporate income, without making provision for consolidation so that the tax could be based upon the income as a whole.

Second. The net profits were not taxable to the company as income of 1916. For the company was not required in 1916 to report as income an amount which it might never receive. See *Burnet* v. *Logan,* 283 U. S. 404, 413. Compare *Lucas* v. *American Code Co.,* 280 U. S. 445, 452; *Burnet* v. *Sanford & Brooks Co.,* 282 U. S. 359, 363. There was no constructive receipt of the profits by the company in that year, because at no time during the year was there a right in the company to demand that the receiver pay over the money. Throughout 1916 it was uncertain who would be declared entitled to the profits. It was not until 1917, when the District Court entered a final decree vacating the receivership and dismissing the bill, that the company became entitled to receive the money. Nor is it material, for the purposes of this case, whether the company's return was filed on the cash receipts and disbursements basis, or on the accrual basis. In neither event was it taxable in 1916 on account of income which it had not yet received and which it might never receive.

Third. The net profits earned by the property in 1916 were not income of the year 1922—the year in which the litigation with

the Government was finally terminated. They became income of the company in 1917, when it first became entitled to them and when it actually received them. If a taxpayer receives earnings under a claim of right and without restriction as to its disposition, he has received income which he is required to return, even though it may still be claimed that he is not entitled to retain the money, and even though he may still be adjudged liable to restore its equivalent. See *Board* v. *Commissioner of Internal Revenue*, 51 F. (2d) 73, 75, 76. Compare *United States* v. *S. S. White Dental Manufacturing Co.*, 274 U. S. 398, 403. If in 1922 the Government had prevailed, and the company had been obliged to refund the profits received in 1917, it would have been entitled to a deduction from the profits of 1922, not from those of any earlier year. Compare *Lucas* v. *American Code Co., supra.*

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.